ABDUL RAHIM BIN SYED MOHD

v.

**RAMAKRISHNAN KANDASAMY;
WAN AHMAD AZLAN BIN WAN MAJID & ANOR.
(INTERVENERS)**

HIGH COURT MALAYA, KUALA LUMPUR
DATO' DR VISU SINNADURAI J
[CIVIL SUIT NO: S4-22-758-1993]
28 JUNE 1996

CONTRACT: *Sale and purchase of land - Standard form used by estate agent - Memorandum of understanding - Legal nature and effect of memorandum of understanding - Construction of document - Whether memorandum of understanding is a legally binding contract for sale and purchase of property - 'Subject to contract' agreement - Inchoate agreement - Factors normally taken into account in property transactions - Whether time is of the essence.*

LAND LAW: *Sale of land - Caveat - Whether signing of memorandum of understanding confers purchaser with caveatable interest.*

WORDS & PHRASES: *'Lock-out' agreement.*

The defendant who is the owner of a piece of property in Kuala Lumpur ('the property') gave a mandate to an estate agent to sell the property. The estate agent found an interested purchaser ('the plaintiff)' for the property at the purchase price of RM550,000 ('the purchase price'). A memorandum of understanding ('MOU'), which was in a standard form with the relevant particulars inserted in the blank spaces, was signed by both parties on 27 September 1993. In accordance with the MOU, an earnest deposit of 1% of the purchase price was paid by the plaintiff on the same day. The plaintiff then entered a private caveat over the property.

It was agreed in the MOU, *inter alia*, that the balance (9%) of the deposit of the purchase price was to be paid by the plaintiff upon the signing of a formal sale and purchase agreement on or before 8 October 1993, and that the balance (90%) of the purchase price was to be paid within 90 days from the signing of the same, with an additional grace period of 30 days if so required by the plaintiff.

The plaintiff, however, did not sign the formal sale and purchase agreement by 8 October 1993. He did so only three days later, ie, on 11 October 1993. On the same day, the plaintiff deposited the balance (9%) of the deposit with his solicitors, as stakeholders, but gave no notice of this to the defendant.

In the result, the defendant refused to sign the formal sale and purchase agreement on the ground that the plaintiff did not sign the same by the stipulated date, ie, 8 October 1993. The defendant then sold the property to another party, *viz*, the interveners in the civil suit.

Consequently, the plaintiff sued the defendant for specific performance of the sale and purchase of the property, claiming that upon the signing of the MOU, a legally binding contract for the sale and purchase of the property had come into force. The defendant in turn filed an originating summons for the removal of the private caveat lodged by the plaintiff over the property. By an order of the Court, the said originating summons was consolidated to be heard together with the civil suit.

Three issues fell for determination before the Court: (i) whether there was a binding contract of sale and purchase of the property between the plaintiff and the defendant; (ii) even if there was, whether the plaintiff's failure to sign the formal sale and purchase agreement on or before 8 October 1993 entitled the defendant to terminate the agreement; and (iii) whether the plaintiff had a caveatable interest in the property.

Held:

[1] A transaction for the sale and purchase of land is not a simple matter. It needs professional attention. As such, most potential purchasers will not give a firm commitment to purchase property at the time they view the property. As a general rule, the purchaser's acceptance will be a conditional one, and it is a fundamental principle of the law of contract that a conditional or qualified acceptance of an offer does not bring about a legally binding contract.

[2] There is a general reluctance on the part of the Courts to give full legal effect to any preliminary arrangement entered into between parties, until it is satisfied that all the detailed terms have been spelt out and agreed upon. Agreements which are merely preparatory to the execution of a formal and detailed agreement, or agreements which merely spell out a general intention of the parties to enter into a contract for the sale and purchase of property are said to be inchoate agreements until the execution of the formal agreement.

[3] Each case must be decided on its own facts. This is especially so in cases dealing with preparatory agreements where the intentions of the parties play a crucial role. In each case, it is the duty of the Court to determine, not only the nature of the document, but also the true intentions of the parties at the time the document was executed.

[4] In the present case, the plaintiff, on viewing the property, expressed an interest in purchasing it. He had, at that stage, made no survey or

technical inspection of the house, nor did he conduct any search on the title to determine whether there were any existing encumbrances on the land or whether there were any special restrictions on the title regarding transfer. More importantly, at that stage, he had made no financial arrangements to secure a loan for the purpose of settling the purchase price which was well over half-a-million ringgit.

[5] If the plaintiff's contention, that an immediately binding contract came into existence on the date of the signing of the MOU, is accepted, the plaintiff will find himself in grave difficulties if, for example, he is unable to raise the necessary funds to pay the purchase price within the stipulated time, or if the plaintiff's solicitors subsequently discover that the defendant's title to the land is subject to restrictions or that the existing encumbrances created by the defendant cannot be discharged, or if it is discovered that the defendant is not the sole proprietor of the land or that he is merely a trustee or a legal representative. In any of these circumstances, the plaintiff may not wish to proceed with the sale. And yet, if the plaintiff's contention is upheld, and if he decides not to proceed with the purchase, the plaintiff will be in breach of contract, enabling the defendant to sue the plaintiff for damages. Clearly, such was not the intention of the parties.

[6] Considering the MOU as a whole, and in particular, its objectives and the 'genesis of the agreement', as well as the intention of the parties at the time of the signing, the MOU was not a legally binding agreement. It was no more than an agreement to negotiate, and as such, it was unenforceable.

[7] A legally binding agreement, therefore, can only come into force upon the execution of the formal sale and purchase agreement, by which time, the parties will have considered all aspects of the sale in detail. Until the execution of the formal agreement, the parties are at liberty to resile from the so-called agreement without any legal consequences. This clearly appeared to be the intention of the parties at the time they signed the MOU, and that, certainly, was the effect of the MOU in law.

[8] Time, in a contract for the sale of land, is of the essence in two situations, *viz:* (i) where the intention of the parties is such that time is of the essence of the contract for the fulfilment of their respective obligations; and (ii) the nature of the subject matter or of the surrounding circumstances are such that the time specified for the performance is of the essence. Other than in these two circumstances, time, in a contract for the sale of land, is not of the essence.

[9] The mere stipulation of a date for completion in a contract does not, by itself, make time to be of the essence of the contract. The nature of

the property and the surrounding circumstances will still have to be considered.

[10] In the present case, time was clearly of the essence, in view of the fact that: (i) the MOU stipulated a deadline for the signing of the sale and purchase agreement; (ii) there was no provision for any grace period for the payment of the the deposit; and (iii) the nature of the property, and more specifically, the nature of the MOU itself which was an initial contract to bring into effect a subsequent main contract for the sale of the property. Thus, even if the MOU is regarded as a binding contract, the failure on the part of the plaintiff to pay the balance of 9% of the deposit and to execute the sale and purchase agreement by 8 October 1993 entitled the defendant to repudiate the contract.

[11] In view of the fact that there was no binding contract between the plaintiff and the defendant under the MOU (and even if there was one, the plaintiff was in breach of the contract in not fulfilling the conditions stipulated in the MOU), the plaintiff had no caveatable interest in the land.

Obiter dicta:

[1] The MOU in the present case was unprofessionally drafted, quite obviously with no legal advice. The use of such documents by estate agents ought to be discouraged, and estate agents should seek legal advice before drafting such documents in the future. An 'option agreement' which contains detailed terms of the sale and purchase, and whereby the purchaser pays a small consideration, is more appropriate. An express clause should also be inserted into the option agreement to spell out the consequence in the eventuality that the purchaser elects not to exercise the option, eg, any moneys (all or part thereof) paid to the vendor will be forfeited, and that neither party will be liable thereafter.

[2] Alternatively, parties should be encouraged to enter into a 'lock-out' agreement. Such an agreement which is not well-known in Malaysia but which has recently gained recognition in England, provides the purchaser some protection.

[3] A 'lock-out' agreement is an agreement which is entered into by a potential purchaser and a vendor of real property whereby the vendor, for good consideration, agrees for a specified period of time, not to negotiate with anyone except the potential purchaser on the sale of his property in which the potential purchaser has expressed an interest.

[Plaintiff's action dismissed; defendant's application for removal of the caveat allowed]

Cases referred to:

Ayer Hitam Tin Dredging Malaysia Bhd. v. YC Chin Enterprise Sdn. Bhd. [1994] 2 MLJ 754 ***(foll)***

Turiff Construction Ltd. & Turiff Ltd. v. Regalia Knitting Mills Ltd. [1971] 9 BLR 20 ***(cit)***

Walford v. Miles [1992] 1 All ER 453 ***(cit)***

Daiman Development Sdn. Bhd. v. Mathew Lui Chin Teck & Anor. [1981] 1 MLJ 56 ***(cit)***

Luggage Distributors (M) Sdn. Bhd. v. Tan Hor Teng & Anor. [1995] 1 MLJ 719 ***(cit)***

Wisma Sime Darby Sdn. Bhd. v. Wilson Parking (M) Sdn. Bhd. [1966] 2 MLJ 81 ***(cit)***

Low Kar Yit v. Mohamed Isa [1963] MLJ 165 ***(cit)***

Masters v. Cameron [1954] 91 CLR 353 ***(cit)***

Diamond Peak Sdn. Bhd. & Anor. v. Tweedie [1982] 1 MLJ 97 ***(cit)***

Lim Keng Siong & Anor. v. Yeo Ah Tee [1983] 2 MLJ 39 ***(cit)***

Von Hatzfelt-Wildenburg v. Alexander [1912] 1 Ch. 284 ***(cit)***

Kam Mah Theatre Sdn. Bhd. v. Tan Lay Soon [1994] 1 MLJ 108 ***(cit)***

Koh Peng Moh v. Yahiya [1965] MLJ 230 ***(cit)***

Koh Peng Moh v. Tan Chwee Boon [1962] MLJ 353 ***(cit)***

Choo Si Seng v. Lee Boon Sai [1986] 1 MLJ 466 ***(cit)***

Tai Tong Realty Co (Pte) Ltd. v. Galstaun & Anor. [1973] 2 MLJ 95 ***(cit)***

Aberfoyle Plantations Ltd. v. Khaw Bian Cheng [1960] MLJ 47 ***(cit)***

Karuppannan Chellapan v. Balakrishnen Subban & Others [1995] 1 SCR 19 ***(cit)***

Pitt v. PHH Asset Management Ltd. [1993] 3 All ER 961 ***(cit)***

Jamshed K Irani v. Burjorji Dhunjibhai [1915] LR 43 1A 26 ***(cit)***

Yeo Kim Pong Realty Ltd. v. Ng Kim Peng [1962] MLJ 118 PC ***(refd)***

Warren v. Tay Sang Geok [1965] 1 MLJ 44 PC ***(cit)***

Koh Shey Guan v. Lee Koh Chen [1971] 1 MLJ 79 FC ***(cit)***

Ayadurai v. Lin Hye [1959] MLJ 143 ***(cit)***

Goh Hooi Yin v. Lim Teong Ghee [1990] 3 MLJ 23 ***(cit)***

Ganam Rajamany v. Samoo Sinnjoh [1984] 2 MLJ 290 ***(refd)***

Loh Boon Siew v. Chin Kim & Anor. [1972] 1 MLJ 139 ***(cit)***

Jaafar bin Ibrahim v. Gan Kun Kin [1985] 2 MLJ 24 FC ***(cit)***

Perri v. Coolangatta Investment Pty Ltd. [1982] 56 ALJR 445 ***(refd)***

Central Malaysia Development Ltd. v. Chin Pak Chin [1967] 2 MLJ 174 ***(cit)***

Legislation referred to:

Contracts Act 1950, s. 7, 30, 56(1), (2)
Contract Act (India), s. 55
Housing Developers (Control and Licensing) Act 1966
National Land Code
Specific Relief Act 1950, s. 20(1)(c)

Other source referred to:

Law of Contract in Malaysia and Singapore, Sinnadurai, 2nd Edn., pp. 588-603

For the plaintiff - Saseedaran Achan; M/s. Achan & Co.
For the defendants - Sri Dev Nair (AS Chandra Segaram with him); M/s. Ram Rais & Partners
For the interveners - M/s. Wan Majid, Mano & Nada

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JUDGMENT

Visu Sinnadurai J:

Introduction

b This Court is called upon to construe a document, commonly referred to amongst estate agents in this country as a memorandum of understanding. I am given to understand that the true legal nature and effect of such a document has not been determined by the Malaysian Courts in any earlier case.

This so-called memorandum of understanding is a document usually prepared
c by an estate agent by way of a standard form contract and is executed by a potential purchaser on the one part, and by a vendor on the second part. On viewing a property which has been advertised for sale, and a purchaser in expressing an interest to purchase the property, estate agents who have the mandate of a vendor to sell the vendor's property, generally request a
d prospective purchaser to sign this document. Such was the position in the present case.

Facts

In the main civil suit, the plaintiff **(the purchaser)** brought an action against
e the defendant, the vendor for specific performance of a contract for the sale and purchase of a house. Based on the so-called memorandum of understanding (MOU) mentioned above, the plaintiff claims that a legally binding contract came into force whereby the defendant agreed to sell the property to the plaintiff.

f In pursuance of this so-called agreement, the plaintiff entered a private caveat over the said land. In the originating summons commenced by the defendant, as applicant, which matter was consolidated with the main civil suit, the defendant applied to this Court for the removal of the said caveat entered into by the plaintiff.

g As will be seen subsequently, the defendant did not complete the sale to the plaintiff, but instead sold the said property to a third party who are now the interveners in the main civil suit.

The salient facts of the present case are as follows: The defendant (**the**
h **vendor**), who is the owner of a piece of property known as Lot 45284, Mukim Kuala Lumpur, Daerah Wilayah Persekutuan, No. 23, Jalan Setia Bakti, Bukit Damansara, Kuala Lumpur, gave a mandate to a housing agent to sell the property. On the introduction of the agent, the plaintiff, who is the prospective purchaser (for convenience I shall refer to the plaintiff as **the purchaser**),
i on viewing, the said property, expressed an interest in purchasing the property. The purchase price was said to be RM550,000. About a week later, the purchaser was asked to sign the memorandum of understanding and the

purchaser agreed to pay an earnest deposit of 1% of the purchase price on 27 September 1993, and further agreed to pay 9% of the purchase price upon the signing of a formal sale and purchase agreement on or before 8 October 1993.

It was further stated in the memorandum of understanding that the purchaser will pay the balance of the 90% of the price within 90 days of the signing of the formal sale and purchase agreement. It was also provided for in the memorandum of understanding that the purchaser would be given a further grace period of 30 days from the said 90 days period to pay the remaining 90% of the purchase price. In other words, the purchaser was to pay the balance of the 90% of the purchase price within a period of 120 days from the signing of the formal sale and purchase agreement.

In accordance with the MOU, the so-called deposit of 1% of the purchase price amounting to RM5,500 was paid by the purchaser to the vendor on 27 September 1993. However, the purchaser did not sign the formal sale and purchase agreement on 8 October 1993 as stated in the memorandum of understanding, but on 11 October 1993. On 11 October 1993, the purchaser also deposited the balance of the 9% of the deposit with his solicitors, as stakeholders, but gave no notice of it to the vendor.

The defendant, the vendor, however, did not sign the formal sale and purchase agreement on the ground that it was not signed by the purchaser within the time period stipulated in the memorandum of understanding. The vendor then sold the property to another party, who are now the interveners in these proceedings.

As the decision of the Court is based primarily on the so-called memorandum of understanding **(MOU)**, I reproduce below the full text of the MOU. It is in a standard form with particulars of the vendor, the purchaser, the property and the purchase price inserted in the blank spaces. It reads as follows, the words underlined being the words inserted:

Memorandum Of Understanding

This **MEMORANDUM OF UNDERSTANDING** entered upon between **Ramakrishnan a/l Kandasamy** IC No **0396762** residing at No 21, Jalan Terasek Dua, Bangsar Baru, Kuala Lumpur as "the vendor" and **Abdul Rahim bin Syed Mohd** IC No **450216-07-5019** residing at **No. 59, Jalan Telawi, Bangsar Baru, Kuala Lumpur** as "the purchaser" has agreed mutually as follows:

1. That THE VENDOR agrees to sell and THE PURCHASER agrees to buy the said property, Lot No. **45284** Mukim **Kuala Lumpur** Daerah **Wilayah Persekutuan situated at No 23, Jalan Setiabakti, Bukit Damansara, Kuala Lumpur**, in an as is where is condition together with fixtures, fittings and structure thereon free of all encumbrances and with vacant possession upon full payment for a total sum of **RM550.000 (Ringgit Malaysia Five Hundred and Fifty Thousand only)**

2. **Schedule of payment**

i. An earnest deposit of one percent (1%) to be paid on **27 September 1993** as confirmation of purchase.

ii. The balance of nine percent (9%) of the initial deposit to be paid upon signing the Sales and Purchase Agreement (S&P).

iii. The remaining ninety percent (90%) to be paid within Ninety (90) days of signing the Sales and Purchase Agreement.

iv. A further grace period of thirty (30) days extension to be provided with a chargeable interest rate of nine percent (9%) to be mutually agreed upon.

3. All legal expenses, transfer and stamping fees and any other charge in respect to the Sale and Purchase Agreement of the said property are to be borne by the above named PURCHASER.

4. In view of this instruction, the parties above named mutually agree to sign a formal Sale and Purchase Agreement to this agreed sale property and complete the transaction on or before **8th October 1993.**

Dated This: **27 September 1993**

Vendor	:	Sgd	Purchaser	:	Sgd
IC No	:	**0396762**	IC No	:	**450216-07-5019**
Witness	:	Sgd	Witness	:	Sgd
Name	:	**S. Sivagnanam**	Name	:	**N. Thinakay Kumar**
IC No	:	**7872460**	IC No	:	**4195596**

Plaintiff's case

The purchaser's main argument is that upon the signing of the MOU, a binding contract for the sale and purchase of the said property came into existence. As such, it was argued that the defendant was under an obligation to sell the said property to the purchaser. The purchaser therefore seeks specific performance of the said contract.

Defendant's case

The defendant's contention is that there was a no binding contract between the parties for the following reasons:

(i) There was no binding contract between the plaintiff and the defendant as the MOU by itself was not a legally binding contract for the sale and purchase of the property;

(ii) Even if it was, the plaintiff's failure to sign the formal sale and purchase agreement on or before 8 October 1993, as required by the MOU, entitled the defendant to terminate the agreement.

In support of the defendant's contention, the defendant argues that the MOU is only an agreement to enter into a formal agreement, and until the formal sale and purchase agreement was entered into, no binding contract came into existence. For this purpose, the defendant relies on cases where the term "subject to contract", or other similar formulae had been used by the parties.

The Law

Two preliminary observations need to be stressed at the off-set. First, a contract for the sale of land is different, in many ways to that of other contractors. As a consequence, the Courts have formulated certain principles over the years in recognition of these differences. These principles are peculiar to transactions involving sale of land only.

Secondly, it must also be observed that a transaction for the sale of property in Malaysia cannot, usually be completed within a short period of time. This is especially so if the land, the subject matter of the sale, is subject to existing encumbrances. Certain procedural steps would also have to be taken by both the vendor and the purchaser before the sale may be completed. Two main steps which the purchaser needs to take, for example, are: (a) to ensure that any encumbrances or restrictions on the title will not pose any problem in the purchase of the land; and (b) that sufficient funds are available to him so that he is in a position to pay the purchase price within the time schedule as stated by the vendor. If the purchaser has any problems with either of these two matters, quite obviously he cannot proceed, and in most cases would not wish to proceed, with the purchase.

As a consequence, the standard sale and purchase agreement in Malaysia for the sale of a property tends to be rather detailed as it has to incorporate several essential terms. Besides, the basic terms relating to the description of the property; identities of the parties; and the purchase price; other terms which are commonly incorporated in the agreement provide for the vendor's obligation to give a title free from encumbrances; the manner in which the vendor intends to discharge an existing charge on the land; undertakings to be given by solicitors to hold the purchase price as stakeholders until the discharge of any existing charge, and the creation of a new charge, if any, by the purchaser. Provisions are also incorporated for the protection of the vendor's purchaser's, and the chargee's interests pending registration of the transfer from the vendor to the purchaser. It is also not uncommon to make provisions for the entry of a private caveat by the purchaser.

a These terms are essential to give full effect to the sale transaction. In the present case itself, the formal sale and purchase agreement prepared by the purchaser's solicitors, Messrs Tengku Mohamed, Achan and Lim, is nine (9) pages long, incorporating about twenty-one (21) main clauses.

b It is therefore obvious that a transaction for the sale and purchase of land is not a simple matter. It needs professional attention. As such, most potential purchasers would not give a firm commitment to purchase the property at the time they view the property. Purchasers, to protect themselves, would usually insist that a certain grace period be given to them so that they may obtain professional advice, and also to satisfy themselves on certain matters before *c* conclusively agreeing to purchase the property. In other words, a purchaser will not agree to bind himself to a legally binding contract on viewing a property until he has conducted the necessary searches and made financial arrangements for the purchase. Therefore as a general rule, the purchaser's acceptance will be a conditional one. It is a fundamental principle of the law of contract that *d* a conditional or qualified acceptance of an offer does not bring about a legally binding contract: see s. 7 of the Contracts Act.

It is for some of these reasons that there is a general reluctance on the part of the Courts to give full legal effect to any preliminary arrangement entered into by the parties, until it is satisfied that all the detailed terms have been *e* spelt out and agreed to by the parties. Agreements, therefore, which are merely preparatory to the execution of a formal and detailed agreement, or agreements which merely spell out a general intention of the parties to enter into a contract for the sale and purchase of the property, are said to be inchoate agreements, until the execution of the formal agreement. It is in this category of agreements *f* that 'subject to contract' agreements, conditional contracts, option agreements, and the like, fall under. These preliminary arrangements, if embodied in a contract-like document, have sometimes been referred to as a "letter of intent" (per Edgar Joseph Jr SCJ in *Ayer Hitam's* case [1994] 2 MLJ 754, following Fay J in *Turriff Construction Ltd. and Turriff Ltd. v. Regalia Knitting Mills* *g* *Ltd.* [1971] 9 BLR 20); or as "a proposal to enter into a contract"; "or an agreement to agree"; or as in the United States, "an agreement to negotiate in good faith": see generally the observations of Lord Ackner in the House of Lords decision, in *Walford v. Miles* [1992] 1 All ER 453.

h These are all merely devices formulated by parties to agree that they may enter into a legally binding contract in the future. These agreements do not bring about a concluded sale and purchase agreement. Such preliminary agreement, strictly speaking, are merely agreements to enable both parties to further negotiate the terms of the sale and purchase agreement, without any obligation on either party to enter into the final sale and purchase contract. *i* Over the years, these terms, like the grant of an option, conditional contract, subject to contract, and other similar formulae, all of which have their origin in the English conveyancing practice, have gained similar recognition by the

Malaysian Courts. This is largely due to the reason that neither the Contracts Act, nor the National Land Code contains any specific provisions dealing with contracts for the sale of land. Except for the provisions in the Housing Developers (Control and Licensing) Act 1966 and the rules made thereunder, which again, is of limited application, no other specific legislation exists to deal with contracts for the sale of land. It is also often overlooked that though the Torrens system is applicable in Malaysia, the National Land Code, the principal legislation applicable in Malaysia relating to land matters, only deals with the post-contract position pertaining to the sale of land.

Though the true legal effect of option agreements, conditional contracts, and contracts which are subject to contract, or similar formulae have all now, over the years, been clearly established by both English and Malaysian case law, unfortunately, parties, and those who advice purchasers and vendors, like solicitors and estate agents, as in the present case, continue to draft documents in which the legal intention of the parties is not made clear. For example, in recent years, the Courts in Malaysia, have been called upon to determine the legal effect of another form of an arrangement called a "booking *pro forma"* agreement. In *Daiman Development Sdn. Bhd. v. Mathew Lui Chin Teck And Anor.* [1981] 1 MLJ 56, the Privy Council held that such a booking *pro forma* signed by a purchaser remained an inchoate agreement, unless again all the terms of the sale and purchase pertaining to the property are spelt out in the booking *pro forma*. And now, it is yet another document, called a memorandum of understanding, the validity of which is in issue.

In the regard, a principle of law which must also be borne in mind is that where the terms of an agreement are incomplete, the agreement is void for uncertainty: see s. 30 of the Contracts Act; and also the judgment of Lord Ackner in the House of Lord decision in *Walford v. Miles* [1992] 1 All ER 453; and also the recent cases of the Court of Appeal (Malaysia) in *Luggage Distributors (M) Sdn. Bhd. v. Tan Hor Teng and Anor.* [1995] 1 MLJ 719; and *Wisma Sime Darby Sdn. Bhd. v. Wilson Parking (M) Sdn. Bhd.* [1966] 2 MLJ 81. See also s. 20(1)(c) of the Specific Relief Act which provides that specific performance will not be granted if the terms of an agreement are uncertain.

Present Case

As pointed out earlier, the plaintiff's contention is that there was an immediately binding contract for the sale and purchase of the house when the memorandum of understanding was signed by the purchaser. The vendor, however contends that no legally binding contract came into force until the formal sale and purchase agreement was executed on or before October 1993.

Both parties in support of their contention have cited the usual anthology of cases relating to this area of the law: *Low Kar Yit v. Mohamed Isa* [1963] MLJ 165; *Daiman Development Sdn. Bhd. v. Mathew Lui Chin Teck &*

Anor. [1981] 1 MLJ 56; *Masters v. Cameron* [1954] 91 CLR 353; *Diamond Peak Sdn. Bhd. & Anor. v. Tweedie* [1982] 1 MLJ 97; *Lim Keng Siong & Anor. v. Yeo Ah Tee* [1983] 2 MLJ 39; *Von Hatzfelt-Wildenburg v. Alexander* [1912] 1 Ch 284; *Kam Mah Theatre Sdn. Bhd. v. Tan Lay Soon* [1994] 1 MLJ 108; *Koh Peng Moh v. Yahiya* [1965] MLJ 230; *Koh Peng Moh v. Tan Chwee Boon* [1962] MLJ 353; *Choo Si Seng v. Lee Boon Sai* [1986] 1 MLJ 466; *Tai Tong Realty Co. (Pte) Ltd. v. Galstaun & Anor.* [1973] 2 MLJ 95; and *Aberfoyle Plantations Ltd. v. Khaw Bian Cheng* [1960] MLJ 47.

I need not go through these cases, as these are familiar to all. Most of them, in any case, merely apply the same principle of law to the particular facts of the case. It, however, must be stressed that each case must be decided on its own facts. This is especially so in cases dealing with preparatory agreements where the intention of the parties plays a crucial role in determining effect. In each case, it is the duty of the Court determine, not only the nature of the document, but also the true intention of the parties at the time the document was executed: Whether the parties intended to be bound by any contract immediately, or only on the fulfilment of certain conditions, eg the execution of a formal contract.

Recently, the then Supreme Court (now the Federal Court) of Malaysia had the opportunity to review some of these authorities. On my part, I adopt the principles as stated by Edgar Joseph Jr SCJ In *Ayer Hitam Tin Dredging Malaysia Bhd. v. YC Chin Enterprises Sdn. Bhd.* [1994] 2 MLJ 754 (though a case not dealing with the sale of land) explaining also the earlier decision of Peh Swee Chin SCJ in the then Supreme Court in *Kam Kah Theatre Sdn. Bhd v. Tan Lay Soon* [1994] 1 MLJ 108. The observations of Peh Swee Chin SCJ in the *Kam Mah Theatre's* case is also poignant. His Lordship observed (at pages 116 - 117):

> It is settled that the formula of 'subject to contract' gives rise to a strong presumption of the necessity of a further formal contract, 'formal' be it noted, is not to be understood in the common parlance as being just a 'mere formality' of no importance.

I also bear in mind the following *dictum* of Sir Garfield Barwick in the Privy Council decision of *Daiman Development Sdn. Bhd. v. Mathew Lui Chin Teck and Anor.* [1981] 1 MLJ 56 where His Lordship made the following observation (at page 58):

> The question whether parties have entered into contractual relationships with each other essentially depends upon the proper understanding of the expressions they have employed in communicating with each other considered against the background of the circumstances in which they have been negotiating, including in those circumstances the provisions of any applicable law. Where they have expressed themselves in writing the proper construction of the writing against that background will answer the question. The purpose of the construction is *to*

> *determine whether the parties intend presently to be bound to each other or whether, no matter how complete their arrangement might appear to be, they do not so intend until the occurrence of some further event, including the signature of some further document* or the making of some further arrangement. The question is one as to expressed intention and is not to be answered by the presence or absence of any particular form of words. [Emphasis added]

In so saying, I do not discount the fact that in certain exceptional cases where the intention of the parties is clearly established, an immediately binding contract may come into force, even though a formal agreement is to be executed subsequently. As Edgar Joseph Jr SCJ observed in *Ayer Hitam's* case (at page 765):

> True it is that merely because the parties contemplate the preparation of a formal contract, that by itself will not prevent a binding contract from coming into existence before the formal contract is signed.

In the light of the above observations, I now consider the legal effect of the memorandum of understanding. Like a booking *pro forma* in a contract for the sale of property under the Housing Developers (Control and Licensing) Act and the rules made therein, or an option agreement, or any other preliminary arrangement, the legal effect of the memorandum of understanding, which, as stated earlier, is commonly used by estate agents, must be determined in the light of existing legal principles. In so doing, I bear in mind, as stated above, that a transaction for the sale of land is quite different to that for the sale of a book, for example.

In the present case, the purchaser on viewing the property, expressed an interest in purchasing it. He had at this stage made no survey or technical inspection of the house, nor had he conducted any search on the title to determine whether there were any existing encumbrances on the land, or whether there were any special restrictions on the title regarding the transfer of the property. More importantly, at this stage, he had also made no financial arrangements to secure a loan for purposes of settling the purchase price. It ought to be borne in mind that the purchase price was well over half-a-million ringgit.

On the part of the vendor, his intention was clear: to sell the property to whosoever wishing to purchase it, subject to certain conditions being fulfilled, namely the time schedule for the payment of the purchase price. In furtherance of this intention, it was made clear to the purchaser that if the purchaser was wishing to purchase the property, the purchaser must be willing, and be in a position, to pay the purchase price within the time frame as stated in the MOU.

It must also be observed that the memorandum of understanding contains no specific provision as to the effect of non-compliance of it by the parties, nor does it provide that until the specified date, the vendor was under an obligation

not to sell the property to a third party. Further, if the MOU had stated that, in consideration of the vendor promising not to do so, the money paid by the purchaser will be forfeited if the purchaser chooses not to go on with the sale, no difficulties would have arisen.

Time and again, the Courts have stated that much of these problems may be avoided if only the consequences of either party not proceeding with the contract are expressly spelt out in the initial agreement itself. Despite these words of caution, such problems continue to arise.

The plaintiff, under the memorandum of understanding, paid 1% of the agreed purchase price "as confirmation of purchase" on the date he signed the memorandum of understanding, that is 27 September 1993. The memorandum of understanding further provided that the balance of the 9% of the purchase price will be paid within eleven (11) days, thereafter, that is on the date the formal sale and purchase is to be signed. This eleven days grace period is probably given to the purchaser to raise sufficient funds to pay the balance of the 9% of the purchase price, and more importantly for the purchaser's solicitors to prepare the formal sale and purchase agreement. Within this brief period, the solicitors for the purchaser would also have to conduct the relevant searches in the land office, and also to determine the manner in which the vendor is proposing to discharge the existing charge over the land so as to enable the vendor to give the purchaser a title free from encumbrances. As to the duties of the purchaser's solicitors, see the recent Federal Court decision in *Karuppannan Chellapan v. Balakrishnen Subban and Others* [1995] 1 SCR 19.

If the purchaser's contention that an immediately binding contract came into existence is accepted, that is on the date of the signing of the memorandum of understanding, the purchaser will find himself in grave difficulties if, for example he is unable to raise the necessary funds to pay the purchase price within the stipulated time, or even if the purchaser's solicitors discover that the vendor's title to the land is subject to certain restrictions, or that the existing encumbrances created by the vendor could not be discharged, or even if it is discovered that the vendor is not the sole proprietor of the land or that he is merely a trustee, or a legal representative.

It must be emphasised that the memorandum of understanding does not even state that the defendant is the registered proprietor of the land, nor give a description of the title.

There may also be other terms which may not be acceptable to the purchaser. In any of these circumstances, the purchaser may not wish to proceed with the sale any further. And yet, if the purchaser's contention is upheld, and if he decides not to proceed with the purchase, the purchaser will be in breach of contract enabling the vendor to sue the purchaser for damages. Clearly such was not the intention of the parties.

It appears to me that considering the memorandum of understanding as a whole, and in particular, in considering the objective of the MOU, and particularly the "genesis of the agreement", and the intention of the parties at the time of the signing of the memorandum of understanding, the memorandum of understanding is not a legally binding agreement. It is no more than an agreement to negotiate, and as such, it is unenforceable.

A legally binding agreement, therefore could only come into force upon the execution of the formal sale and purchase agreement, by which time the parties would have considered all aspects the sale in detail and a formal agreement prepared by the solicitors to cover all these aspects of the sale, for execution. Until the execution of the formal agreement, as there is no binding contract between the parties, the parties are at liberty to resile from the so-called agreement, without an legal consequences flowing from such an action. Such clearly appears to be the intention of the parties at the time of the signing of the memorandum of understanding, and that certainly is the effect of the memorandum of understanding in law.

I am further fortified with the view that I have taken when I consider some of the terms which are embodied in the formal sale and purchase agreement prepared by the plaintiff's solicitors, especially clauses (1) and (12).

Clause 1 of the formal sale and purchase agreement expressly provides that a deposit will only be paid by the purchaser on the signing of the formal sale and purchase agreement, which deposit, under clause 4.1 would be forfeited if the purchaser should default in the payment of the balance of the purchase price within the time stipulated. A distinction is drawn between the first payment of RM5,500 which is termed as earnest money, and the full ten percent of RM55,000 as a deposit. The vendor has the right to forfeit the deposit, but not the earnest money which had been paid before the execution of the formal sale and purchase agreement. Furthermore, under clause 12 of the draft sale and purchase agreement, the purchaser is entitled to enter a private caveat only after the payment of the full 10% of the purchase price as deposit, that is, after the execution of the sale and purchase agreement. It was therefore impliedly agreed that the purchaser had no right to enter a private caveat on the signing of the MOU, therefore indicating that the MOU was not intended to bring into force a legally binding contract until the execution of the formal sale and purchase agreement.

In passing I would observe that the MOU is a document which is unprofessionally drafted, quite obviously with no legal advice. It is my view that the use of such documents by estate agents ought to be discouraged, and that estate agents should seek legal advice before drafting such documents in the future. An option agreement, whereby the purchaser pays a small consideration, and one which contains detailed terms of the sale and purchase, appears to be more appropriate. Such an option agreement, will give the

purchaser reasonable time to consider, after making all the necessary inquiries and searches, whether to commit himself to the purchase. On the other hand, the vendor will be under an obligation, in view of the consideration paid, not to sell the property to a third party until after the expiration of the option period. An express clause should also be inserted in the option agreement to spell out the consequence in the eventuality the purchaser elects not to exercise the option, that is, any monies (all or part thereof) paid to the vendor will be forfeited, and that neither party will be liable thereafter

Alternatively, parties should be encouraged to enter into a lock-out agreement. Such an agreement, which is not well-known in Malaysia and which has gained recognition in England only recently, provides the purchaser some protection.

A lock-out agreement is an agreement which is entered into by a potential purchaser and a vendor of real property whereby the vendor for good consideration agrees for a specified period of time, not to negotiate with anyone except the potential purchaser in relation to the sale of his property in which the potential purchaser has expressed an interest in purchasing. Such an agreement was given judicial recognition by the House of Lords in *Walford v. Miles* [1992] 1 All ER 453, and subsequently applied by the Court of Appeal in *Pitt v. PHH Asset Management Ltd.* [1993] 3 All ER 961. Lord Ackner (in *Walford's* case) in holding a lock-out agreement to be enforceable said (at page 461):

> There is clearly no reason in English contract law why **A**, for good consideration, should not achieve an enforceable agreement whereby **B** agrees for a specified period of time not to negotiate with anyone except **A** in relation to the sale of his property.

His Lordship further added:

> There are often good commercial reasons why **A** should desire to obtain such an agreement from **B**. **B**'s property which **A** contemplates purchasing may be such as to require the expenditure of not inconsiderable time and money before **A** is in position to assess what he is prepared to offer for its purchase or whether he wishes to make any offer at all. **A** may well consider that he is not prepared to run the risk of expending such time and money unless there is a worthwhile prospect, should he desire to making offer to purchase, of **B**, not only then still owning the property, but of being prepared to consider his offer. **A** may wish to guard against the risk that, while he is investigating the wisdom of offering to buy **B**'s property, **B** may have already disposed of it or, alternatively, may be so advanced in negotiations with a third party as to be unwilling or for all practical purposes unable to negotiate with **A**.

There are two essential elements in a lock-out agreement: (a) the agreement must contain a negative undertaking; and (b) it must be for a fixed duration. Such a lock-out agreement is treated as collateral contract, if a subsequent contract is entered into between the parties. As a lock-out agreement is an

independent and binding agreement, a breach of the lock-out agreement by the vendor will entitle the purchaser to sue for damages.

It therefore appears to me that one of the most appropriate means of preventing a vendor from "gazumping", that is, in attempting to sell the property at a higher price subsequently, is for the purchaser to give a small consideration for the vendor's promise not to sell the property to a third party for a specified period. The giving of such consideration, will ensure to the purchaser, that the vendor is under an obligation not to sell the property to anyone else but the purchaser; whereas, the purchaser is under no obligation to purchase the property. It must be stressed, that by this arrangement, neither party has committed himself to a legally binding contract for the sale of the property. All that has been agreed is that, the vendor will not sell the property to a third party during the specified time.

Finally, as a word of caution, in cases where parties still choose to enter into a conditional contract, or a subject to contract agreement, the parties ought to advised to state expressly in the document that in that event of any failure of the part of either party to fulfill their specified obligations, certain specific consequences will follow: the forfeiture of any deposit paid; or the termination of the agreement with or without any other legal consequences.

Conclusion on the MOU

I therefore hold that by the signing of the MOU itself, no binding contract came into effect between the plaintiff and the defendant. In other words, I hold that the MOU falls within the category of agreement which are not legally enforceable.

The plight of the purchaser in the present case is no different to that of many other purchasers, or even that of vendors in some cases, who enter into such agreements. Such a position of many a vendor or a purchaser is aptly described by Sir Thomas Bingham, MR (as he then was) in *Pitt v. PHH Asset Management Ltd.* [1993] 3 All ER 961. This is what he said (at page 967).

> For very many people their first and closest contact with the law is when they come to buy or sell a house. They frequently find it a profoundly depressing and frustrating experience. The vendor puts his house on the market. He receives an offer which is probably less than his asking price. He agonises over whether to accept or hold out for more. He decides to accept, perhaps after negotiating some increase. A deal is struck. Hands are shaken. The vendor celebrates, relaxed, makes plans for his own move and takes his house off the market. Then he hears that the purchaser who was formerly pleading with him to accept his offer has decided not to proceed. No explanation is given, no apology made. The vendor has to embark on the whole dreary process of putting his house on the market all over again.

> For the purchaser the process is, if anything, worse. After a series of futile visits to unsuitable houses he eventually finds the house of his dreams. He makes an offer, perhaps at the asking price, perhaps at what the agent tells him the vendor is likely accept. The offer is accepted. A deal is done. The purchaser instructs solicitors to act. He perhaps commissions an architect to plan alterations. He makes arrangements to borrow money. He puts his own house on the market. He makes arrangements to move. He then learns that the vendor has decided to sell to someone else, perhaps for the price already offered and accepted, perhaps for a increased price achieved by a covert, unofficial auction. Again, no explanation, no apology. The vendor is able to indulge his self-interest even his whims, without exposing himself to any legal penalty.

Finally, as there is no mention in the memorandum of understanding as to the effect of the 1% of the purchase price deposit paid by the purchaser on the signing of the MOU, in the eventuality that a formal sale and purchase agreement is not entered into, and as the MOU is not a binding contract, the said sum ought to be refunded to the purchaser.

Time

The second argument raised by the defendant, the vendor, is that even if the memorandum of understanding was a valid and legally binding agreement, as time was of the essence of the agreement, the failure on the part of the purchaser to pay the balance of the purchase price on 8 October 1993, constituted a breach of the agreement which entitled the vendor to terminate the agreement.

On this issue, the plaintiff's counter-argument is as follows: That time was not of the essence of the contract, even though the MOU states that the formal sale and purchase agreement must be executed before 8 October 1993.

In Malaysia, the law relating to time for the performance of obligations by parties under a contract is provided for in s. 56 of the Contracts Act. Of particular importance is s. 56(1) which provides as follows:

> When a party to a contract promises to do a certain thing at or before a specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of the essence of the contract.

The Privy Council, in interpreting similar provisions under the Indian Contract Act, has held that this section gives statutory effect to the English rule relating to time. Viscount Haldane in the case of *Jamshed K Irani v. Burjorji Dhunjibhai* [1915] LR 43 1A 26, observed of s. 55 of the Indian Contract Act (s. 56 of the Malaysian Act):

> Their Lordships do not think that this section lays down any principle which differs from those which obtain under the law of England as regards contracts to sell land.

This interpretation of s. 56 has subsequently been adopted by the Malaysian Courts in several cases: see Sinnadurai, *Law of Contract in Malaysia and Singapore*, 2nd edition, pages 588-603.

Therefore, under the Contracts Act, as well as under English law, time, in a contract for the sale of land, is of the essence in two main situations: (i) where the intention of the parties was such that time was of the essence of the contract for the fulfilment of their respective obligations; and (b) the nature of the subject matter, or the surrounding circumstances are such that time specified for the performance is of the essence. Other than under these two circumstances, time in a contract for the sale of land, is not of the essence.

There is little difficulty in considering whether time is of the essence of a contract if there is an express provision in the contract itself stating that it is so. In contracts where the phrase "time is of the essence" is employed, it is generally accepted that the parties in these cases have clearly intended that the provision dealing with time is an essential term of the contract. In such cases, both parties must perform their respective obligations within the time stipulated. If either party fails to do so, the other party, under s. 56(2) of the Contracts Act is entitled to repudiate the contract.

Where there is no express provision in the contract making time of the essence, the Courts will then have to consider the nature of the property, the surrounding circumstances and the nature of the contract, to determine whether time was intended by the parties to be the essence of the contract. In *Yeow Kim Pong Realty Ltd. v. Ng Kim Peng* [1962] MLJ 118 PC, though, time was not expressly stated to be of the essence, it was held that considering the intention of the parties, and on an "examination amongst other things of attendant circumstances", time was of the essence of the contract in question. But in the following cases, for example, where there was a no express provision making time of the essence, time was held not to be of the essence: *Warren v. Tay Sang Geok* [1965] 1 MLJ 44 PC; *Koh Shey Guan v. Lee Koh Chen* [1971] 1 MLJ 79 FC; *Ayadurai v. Lin Hye* [1959] MLJ 143; and *Goh Hooi Yin v. Lim Teong Ghee* [1990] 3 MLJ 23.

It should be emphasised that as pointed out by the Federal Court in *Ganam Rajamany v. Samoo Sinnjoh* [1984] 2 MLJ 290, the mere stipulation of a date fixed for completion in a contract, does not, by itself make time to be of the essence of the contract. The nature of the property, and the surrounding circumstances would still have to be considered in such cases.

In the light of the above principles, I now move on to consider whether time was of the essence of the contract entered into between the plaintiff and the defendant.

The MOU expressly stipulates that a formal sale and purchase agreement had to be executed and that the sale transaction completed "on or before 8 October 1993". Of course, as stated earlier, this stipulation by itself does not make time of the essence of the contract. Other factors need to be considered. Under the MOU, there is a schedule of payment providing that 1% of the purchase price was to be paid on 27 September 1993, the balance 9% to be paid on or before 8 October 1993, that is, on the execution of the formal sale and purchase; and the remaining balance of 90% within 90 days from the signing of the sale and purchase agreement. As regards this last payment, the MOU provides for a further grace period of 30 days. There is no mention of any grace period for the payment of the first two payments, clearly therefore envincing an intention on the part of both parties that time was of the essence for the payment of these two payments.

Further, in considering the nature of the property and more specifically the nature of the MOU itself, it appears to me that time is of the essence of the contract. This is a preliminary agreement between the two parties for the sale and purchase of the property. The first two payments relate to the payment of a deposit to indicate the earnestness of the purchaser to go on with the contract. Clearly what was in the mind of the vendor was that if the purchaser was not in a position, or was unwilling to comply with the schedule of payment and the signing of the formal sale and purchase agreements within the specified period, the vendor would no longer wish to be bound by the contract. The vendor had clearly stated in evidence that he wished to sell the property as he needed the money. Similarly, the purchaser had also indicated that he needed a house to live in. Therefore, there was a clear intention on the part of both parties to complete the sale as scheduled. Their intention was clearly to make time of the essence of this contract.

There is yet another reason as to why I take the view that time was of the essence of the contract. This MOU, like an option agreement or a conditional contract, deals with the initial stages of a sale transaction. As stated earlier, it is in the nature of a "letter of intent". Unlike other contracts which have been partly executed, much the obligations remain outstanding under the MOU. The parties, under the MOU are still in the stage of having only entered into an initial contract to bring into effect a subsequent main contract for the sale of the property, which contract will incorporate all the other duties and obligations of the parties. Until this initial contract is concluded, the main contract for the sale of the property cannot be fully executed. In such types of initial contracts, time is generally of the essence. It is for this reason that in option agreements, time is generally considered to be of the essence: *Loh Boon Siew v. Chin Kim and Anor*. [1972] 1 MLJ 139.

Similarly, in conditional contracts, where the contract of sale fixes a date for performance of a particular condition, the Courts have held that time being of the essence, that condition ought to be fulfilled by that date: see generally the principles spelt out by Lord Jenkins in *Aberfoyle Plantations Ltd v. Khaw Bian Cheng* [1960] MLJ 47 PC; *Jaafar bin Ibrahim v. Gan Kun Kin* [1985] 2 MLJ 24 FC. As to the importance of time in a lock-out agreement, see *Walford v. Miles*, above.

Furthermore, in such cases, where the condition is not promissory in nature but rather contingent, the contingency in the present case being the execution of the sale and purchase agreement before 8 October 1993, equitable principles relating to time do not apply. As Gibbs CJ said in the Australian High Court decision in *Perri v. Coolangatta Investments Pty Ltd.* [1982] 56 ALJR 445, at page 448:

> ... I consider that when the time has elapsed for performance of a condition which is not a promissory condition, but a condition precedent to the obligation to complete a contract of sale, either party, if not in default, can elect to treat the contract as at an end if the condition has not been fulfilled or waived, and that it is not necessary first to give a notice calling on the party in default to complete the contract or fulfil the condition ... the time fixed by the contract for performance of the condition [is] not to be extended by reference to equitable principles.

I may also observe in passing that the draft sale and purchase agreement prepared by the purchaser's solicitors, itself by clause 13 expressly provides that time should be deemed to be of the essence of the agreement.

I therefore conclude that in the present case that even if the MOU is regarded as a binding contract, the failure on the part of the purchaser to pay the 9% of the purchase price, and to execute the sale and purchase agreement on 8 October 1993, entitled the vendor to repudiate the contract. As the obligation was on the purchaser to ensure that both the 9% of the purchase price, and the execution of the formal sale and purchase agreement (at least on his side) was completed by 8 October, his failure to comply with these conditions is fatal to his case. If the purchaser had at least fulfilled his obligation, and if subsequently the vendor had refused to sign the sale and purchase agreement, it would have been a different story. The obligation on the part of the vendor to sign only arises when the purchaser has completed his part of the bargain: see generally s. 52 of the Contracts Act dealing with reciprocal promises and the case of *Central Malaysia Development Ltd. v. Chin Pak Chin* [1967] 2 MLJ 174.

Removal of Caveat

In the originating summons, the vendor applied to remove the caveat entered into by the purchaser. In the light of the view I have taken, that there was no binding contract between the purchaser and the vendor under the MOU,

or that even if there was one, the purchaser was in breach of the contract in not fulfilling the conditions stipulated in the MOU, I hold that the purchaser has no caveatable interest in the land. The vendor's application, under the originating summons, for the removal of the caveat entered into by the purchaser is therefore allowed.

Interveners' Interest

The interveners' interest in this action is relevant only if the purchaser had succeeded in his claim against the vendor. In view of the conclusion I have reached, there is no question of competing interests, or priorities arising between the purchaser and the interveners, and as such the interveners' position remains unaffected by this decision.

Reported by Lee Teng Joo